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BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

EXIGENT REQUEST, 2010	Docket No. R2010-4

**REPLY COMMENTS OF THE
NATIONAL POSTAL POLICY COUNCIL**

Arthur B. Sackler
Executive Director
NATIONAL POSTAL POLICY COUNCIL
750 National Press Building
529 14th Street, N.W.
Washington, D.C. 20004
(202) 955-0097

William B. Baker
WILEY REIN LLP
1776 K Street, N.W.
Washington, DC 20006-2304
(202) 719-7255

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<u>NATIONAL POSTAL POLICY COUNCIL</u>
(September 2, 2010)

The initial comments of the vast majority of mailers and mailer groups demonstrate that the Postal Service's request to raise rates fivefold the rate of inflation is not justified under Section 3622(d)(1)(E) of the Postal Accountability and Enhancement Act of 2006 ("PAEA"). In these reply comments, the National Postal Policy Council ("NPPC") will address certain issues raised by the Public Representative and the American Postal Workers Union ("APWU") regarding the rate structure for First-Class commercial Bulk letters.

Although these reply comments address details of the rate structure, the Commission should not lose sight of the more important issue, which is the great vulnerability of the Postal Service's First-Class Bulk letter mail volumes to electronic diversion. Rate increases of the levels proposed would only accelerate that conversion. Indeed, in the current economic environment, *any* rate increase would be counterproductive for the Postal Service's long term interests.

NPPC's initial comments pointed out how the Postal Service's volume forecasts understate the volume loss it will suffer in First-Class commercial Bulk letters if the requested rates take effect. The Declaration of Arthur B. Sackler attached to NPPC's comments explained that if the rates were to take effect, seven NPPC members alone would expect to reduce their volumes collectively by *more* than the entire amount that the Postal Service forecasts to lose in that entire product.[1] NPPC explained that the Postal Service's forecasting model does not accurately or completely account for the fundamental change in the demand for commercial First-Class letters that occurred during the recent recession.[2]

Increasing First-Class Bulk letter rates will merely accelerate the shift of account statements to electronic alternatives, hastening a permanent reduction in the volume of First-Class Bulk letters – the Postal Service's *most profitable product* -- for years to come. And this reduction would have unmeasured, but likely significant, derivative effects on Single Piece and Standard mail volumes. Once a customer moves to electronic delivery of statements and account information, electronic delivery typically becomes the exclusive means by which a business communicates with that customer. That customer, in turn, makes payments and communicates with the company by nonpostal means.

Rate increases that would be so counterproductive to the Postal Service's own best interests would not be "reasonable and equitable and necessary" or reflect "best practices" of management as required by Section 3622(d)(1)(E) of

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[1] *See* Declaration of Arthur B. Sackler. If the proposed rates take effect, those seven NPPC members alone would expect to reduce their Automation and Presort-rated mail volumes by approximately 344 million letters in 2011 -- a greater volume loss than the Postal Service projects for the *entire product*. The NPPC volume estimate covers Calendar Year 2011, and therefore includes one quarter omitted from the Postal Service's FY 2011 volume forecast period.

[2] *Accord* Comments of the National Association of Presort Mailers on the Rate Adjustments Requested by the United States Postal Service due to Extraordinary or Exceptional Circumstances at 4; Comments of Discover Financial Services at 6.

the PAEA. Accordingly, the requested First-Class Bulk rate increases would violate the law for a reason separate from the Postal Service's failure to satisfy the statutory condition of "extraordinary or exceptional circumstances."

The permanent damage to the Postal Service's First-Class Bulk letter volumes from an exigent rate increase would not be ameliorated by tinkering with the specific rates and passthroughs for 5-digit, 3-digit, AADC Automation, or mixed AADC automation letters as suggested by some commenters.[3] Nonetheless, NPPC is submitting these reply comments in response to certain comments regarding First-Class Bulk letter rate design by the Public Representative and the APWU.[4]

I. THE COMMISSION NEED NOT CONDUCT A SECTION 3622(e) REVIEW OF FIRST-CLASS BULK LETTER RATES IN THIS PROCEEDING

Both the Public Representative and the APWU criticize the Postal Service for proposing what appears to be a 120 percent "passthrough" of the purported cost difference between the Automation Mixed AADC rate and the Automation AADC rate on the grounds that it appears larger than the 110 percent passthrough calculated in the most recent Annual Compliance Determination,

[3] Reducing the rate increases for First-Class Bulk letters to the system average, as Discover suggests (Comments of Discover Financial Services at 3) would not avoid accelerating the shift to electronic diversion. Even such an increase would still greatly exceed the rate of inflation.

[4] NPPC notes that the adjustment suggested by the National Association of Presort Mailers, on the merits of which we take no position, does not address the fundamental problem that any rate increase would accelerate electronic diversion.

which covered FY2009.[5] Public Representative Comments at 52; APWU Comments at 4. They ask for a "plan" or "firm timetable" to "bring the discounts in line with avoidable costs and thus send the appropriate price signals." Public Representative Comments at 53; APWU Comments at 5.

This subject becomes an issue in this proceeding only if the Commission finds that "extraordinary or exceptional circumstances" exist and that rate increases in First-Class Mail are "reasonable, equitable, and necessary" and consistent with "best practices" of management. Furthermore, the Commission is currently conducting a separate rulemaking proceeding to consider the proper relationship of First-Class Single-Piece and Bulk letter rates. Nonetheless, if the Commission were to consider this issue in this proceeding, NPPC respectfully submits that the concerns raised by the Public Representative and the APWU are premature and incorrectly compare costs and rates from entirely different periods of time.[6]

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[5] The Public Representative also criticizes the purported 119.6 percent passthrough for the Automation Mixed AADC rate, although recognizing that the Postal Service's proposed estimated passthrough for that rate is on its face smaller than in the most recent ACD. *See* Public Representative Comments at 52-53. Regarding the Automation Mixed AADC rate, the Commission should keep in mind that any reduction in that discount must take into account Section 3622(e)(3)I The loss of high-margin volume that would follow from any increase in the rates paid by Mixed AADC mail, and the push-up "ladder" effect on all other Automation rates, could threaten such a loss of institutional cost contribution that Single-Piece rates would have to rise still more to make up for the shortfall.

[6] These commenters also make two other fundamental errors. First, they persist in assuming that First-Class Bulk letter product rates must be "linked" to Single-Piece rates. That very issue is currently under review in a separate rulemaking. Second, they assume that rate differences between commercial and Single-Piece letters should not reflect any cost or demand differences other than those that are "worksharing" related. Such an approach gives Automation and Presort mailers no rate credit for the substantially lower cost of their mail, nor does it recognize that their demand differs from that of Single-Piece mailers. On the contrary, the statutorily-required "best management practices" would appear to *require* pricing these separate products on their own merits.

A. A Section 3622(e) Review At This Time Would Be Premature

As NPPC pointed out in its opening comments, there is no need for the Commission to review the proposed rates in light of Section 3622(e) because the appropriate time to do so, if at all, would be during the Annual Compliance Review covering the period for which the rates would be in effect. That would be the Annual Compliance Review for FY2011 and, presumably, FY2012 as well. Considering Section 3622(e) issues now thus would be premature.

The Commission's practice under the PAEA generally is to defer final rulings on the lawfulness of rates until the Annual Compliance Determination. *See* Rule 3010.13(j) (omitting Section 3622(e) from issues to be decided during Type 1 rate adjustment); *Order Reviewing Postal Service Market Dominant Price Adjustments*, Docket No. R2009-2, at 4-6 (Mar. 16, 2009) (not accepting contention that it must reject rates not complying with traditional workshare discount design methodologies pending rulemaking); *Review of Postal Service Notice of Market Dominant Price Adjustment*, Docket No. R2008-1 at 19 (March 17, 2008) (but stating that Commission will reject at review stage a discount passthrough of 557.8 percent). None of the First-Class commercial letter rates proposed by the Postal Service purports to passthrough more than a comparatively modest 120 percent of the ACD costs. Accordingly, there is no need for the Commission to review those rates any further at this time.

Because the Commission's practice is not to review such rate proposals for Section 3622(e) compliance at this time, there is no basis for insisting that the Postal Service provide a "firm timetable" or "plan" for reducing the purported passthroughs. That is because there is no finding, and as explained in the next subsection cannot be a finding, that the rates exceed the "avoided costs." Without such a finding, there is no need for a "plan" or "timetable."

B. The Commission Should Not Compare FY2011 Rates To FY2009 Costs For Section 3622(e) Purposes

Comparing the proposed First-Class Automation rates to the most recent ACD costs, as the Public Representative and APWU ask the Commission now to do, would mix apples and oranges by comparing *FY2011* (and presumably at least the first quarter of FY2012) rates with *FY2009* costs. Never has the Commission relied on a two-year mismatch between costs and rates when considering a Section 3622(e) issue.

The rates proposed in this case would not take effect until January 2, 2011, but the avoided costs to which the Public Representative and APWU ask them to be compared for Section 3622(e) purposes were accrued between October 2008 until September 30, 2009 (the FY2009 period reviewed in the FY2009 ACD). By the time January 2, 2011 arrives, fifteen full months will have elapsed since the end of the 12 months of costs against which they would be compared. Thus, the FY2009 costs relied upon by the Public Representative and APWU would be from 15 to 27 months old when the Automation rates would take effect.

NPPC addressed this issue at some length in its opening comments and will not repeat itself now. What is significant, however, is that neither the Public

Representative nor the APWU consider this mismatch of costs and rates in their comments.[7]

Nor do they take into account that the postal costs avoided quite likely will have increased between September 30, 2009, and January 2, 2011. That reason alone provides ample reason for the Commission to disregard their concerns now. History teaches that postal costs readily could increase enough by that time to make the costs equal to (or even less than) the amount of the discounts that may appear today to exceed avoided costs. APWU offers no evidence that the costs avoided (largely mail processing labor costs) will be getting smaller by 2011, that wage rates will decline, or that the rate differences will not equal or exceed the cost differences in FY2011.

In light of the risk that higher rates will simply drive the highest-margin First-Class Bulk letters out of the mailstream, inevitably resulting in ever-higher Single-Piece rates to make up the difference, the Commission should be extremely wary of drawing premature conclusions about discounts. This is especially important where, as here, the "ladder" effect of reducing the Mixed AADC discount would raise all of the other Automation rates by the same amount, driving them out of the system permanently. The exception contained in Section 3622(e)(3)(A) and (B) of the PAEA exists to prevent such a result, and the principles embodied in that provision counsels the Commission to approach the matter cautiously.

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[7] The Postal Service has already agreed with NPPC that reviewing passthroughs at this time "would result in a timing mismatch." Response of the United States Postal Service To Oral Request at the Hearing on August 122, 2010 (Kiefer) Tr. 3/382 at 5.

The first Annual Compliance Review in which rates resulting from this case would be reviewed will start at the end of 2011. The rates and costs that will serve as the subject of that review will be from Fiscal Year 2011, ending September 30. That would be the appropriate time to consider any Section 3622(e) issues.

II. CONCLUSION

For the reasons set forth in its opening comments and in these reply comments, the National Postal Policy Council respectfully urges the Commission to find that "extraordinary or exceptional circumstances" do not exist, to reject the proposed rate increases for First-Class Bulk letters mail as not reasonable, equitable, or consistent with best business practices, and to defer consideration of Section 3622(e) issues arising from rates in this proceeding until the first Annual Compliance Review in which costs and rates are from the same period of time.

Respectfully submitted,

NATIONAL POSTAL POLICY COUNCIL

By: /s/ William B. Baker

William B. Baker
WILEY REIN LLP
1776 K Street, N.W.
Washington, DC 20006-2304
(202) 719-7255

Arthur B. Sackler
Executive Director
NATIONAL POSTAL POLICY COUNCIL
750 National Press Building
529 14th Street, N.W.
Washington, D.C. 20004
(202) 955-0097

Certificate of Service

I hereby certify that I have this 2d day of September, 2010, caused to be served the foregoing document in accordance with sections 12 and 20(c) of the rules of practice.

William B. Baker____
William B. Baker